DOW THEORY LETTERS INC.

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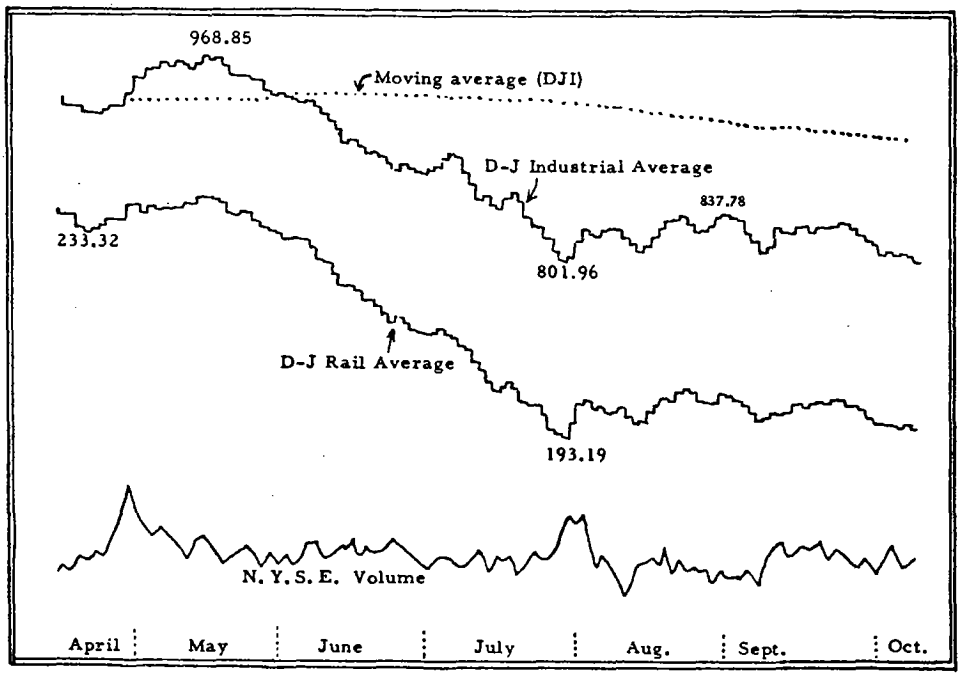
THE MARKET: As seen on the chart below the Industrial Average has launched three attacks on the 840 level. Each of those assaults failed with the highest level having been reached on September 2 at 837.78. During the same period (since July 29, 1969) the Industrials have tried three times to penetrate the 800 level on a closing basis. The lowest they have reached is the 801.96 close of July 29, 1969.

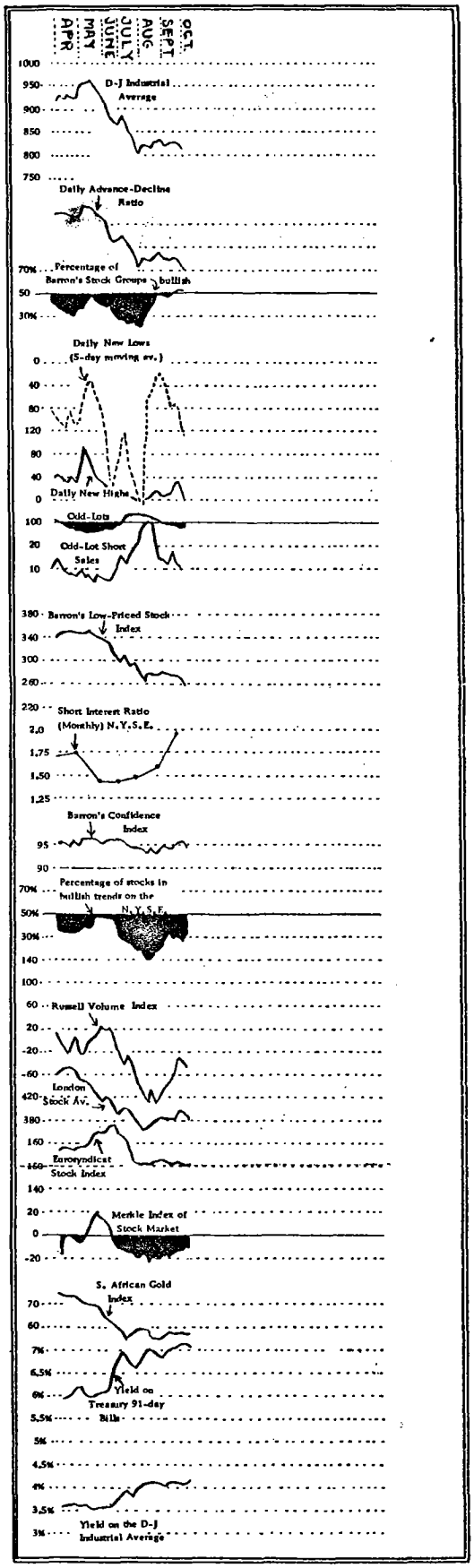
The latest downside attempt was the decline to October 2. On that day Industrials got as low as an inter-day 801.81 (1P.M., New York time). But a rally immediately set in, and by the end of the day Industrials had closed up 4.95 at 808.20.

In the last Letter I discussed the price-breadth relationship, and I want to review that study again. The chart on page 2 brings the Letter 439 chart up-to-date. Note that on the upside we have a non-confirmation where the Advance-Decline ratio failed at peak 2 to better peak 1, even though the Industrial Average at peak 2 (Sept. 1) bettered its August 22 (peak 1) high. This brought on the reaction which continued all through September.

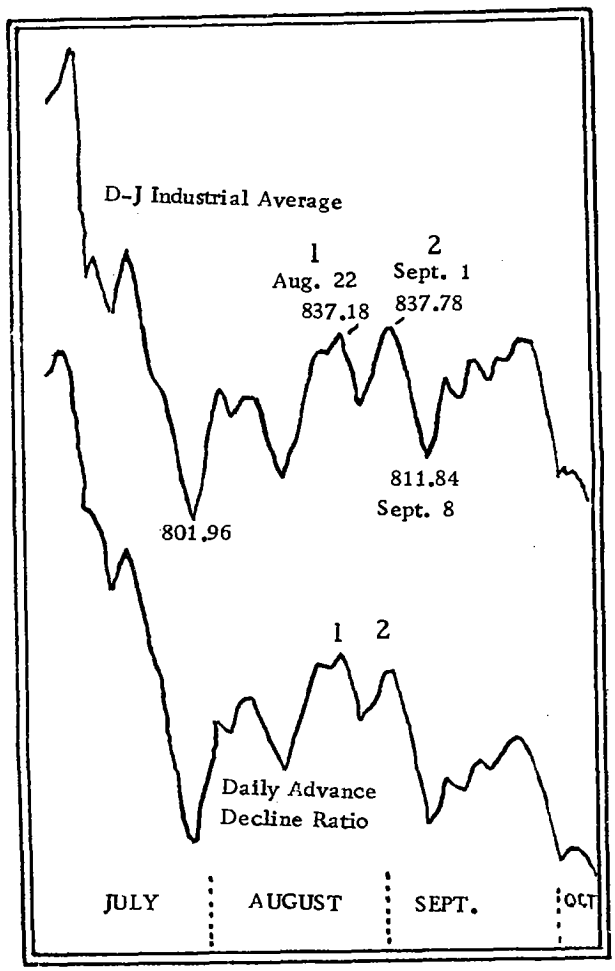
It is important to note that on October 1 the A-D ratio plunged to a new low for 1969. The Industrial Average however, failed to confirm. It held persistently above its 1969 low of 801.96. That non-confirmation set up the rally of October 2 and 3. Thus we have a picture of the Industrial Average which is persistently stronger than the rest of the market. Industrials proved stronger on the upside by rising to a new recovery peak on September 1. Industrials proved stronger on the downside by refusing to confirm a new October, 1969 low in the A-D ratio.

Technically, this leaves the market in a stalemate, but ultimately it is obvious that either the A-D ratio (meaning the majority of stocks) will confirm the strength in the Industrial Average or the Industrial Average will confirm the weakness in the majority of stocks as represented by the A-D ratio.





By sinking to a 1969 low, the A-D ratio confirmed new lows over the past week in the D-J Utility Average and the D-J 40-Bond Average. Odd-lot ratios were trending to less selling on the decline and on October 1 they began a switch to the buying side of the market. Thus the public seems to have concluded that lower prices represent bargain prices and this sentiment is apt to prove wrong. A final consideration is that this is a primary bear market, and during periods of indecision it is correct policy to conclude that the outcome will develop in the direction of the primary trend, which is now down.



I therefore warn subscribers against premature bullishness, even over the near-term, regarding the action of the market since July 29. Because this is a primary bear market it is logical to believe that the narrow price fluctuations since July 29 represented distribution of stocks and that the ultimate outcome will be a penetration of the 800 level and a plunging of the market to new low levels.

On the week ending October 3, Barron's Low-Priced Stock Index recorded a new 1969 low of 258.9. This indicates to me that speculation is gradually waning, that tight money is taking its toll, and that the public and the speculators are slowly but surely on the way to taking huge losses in unseasoned issues. It is a characteristic of the Low-Priced Index to sink persistently during a primary bear market. Rallies in the Low-Priced list become progressively less impressive as a bear market continues. The reason: Speculators are less and less prone to "take a flyer" during each rally, and more and more apt to jump in on quality issues. Ultimately, as the bear market moves towards its bottom, the low-priced "cats-and-dogs" will be a drug on the market.

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As a further consideration, I have just received my latest copy of the authoritative Bank Credit Analyst edited by Donald Storey, and their conclusion is that the underlying bank and credit structure is still very bearish. Particularly bearish are the liquidity ratios, with both bank and corporate liquidity at levels which, as Mr. Storey states it, renders ".....the outlook for stocks and business.....unattractive."

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In the last report I discussed the bear market's toll on corporate dividends. This little news clip tabulates the latest statistics.

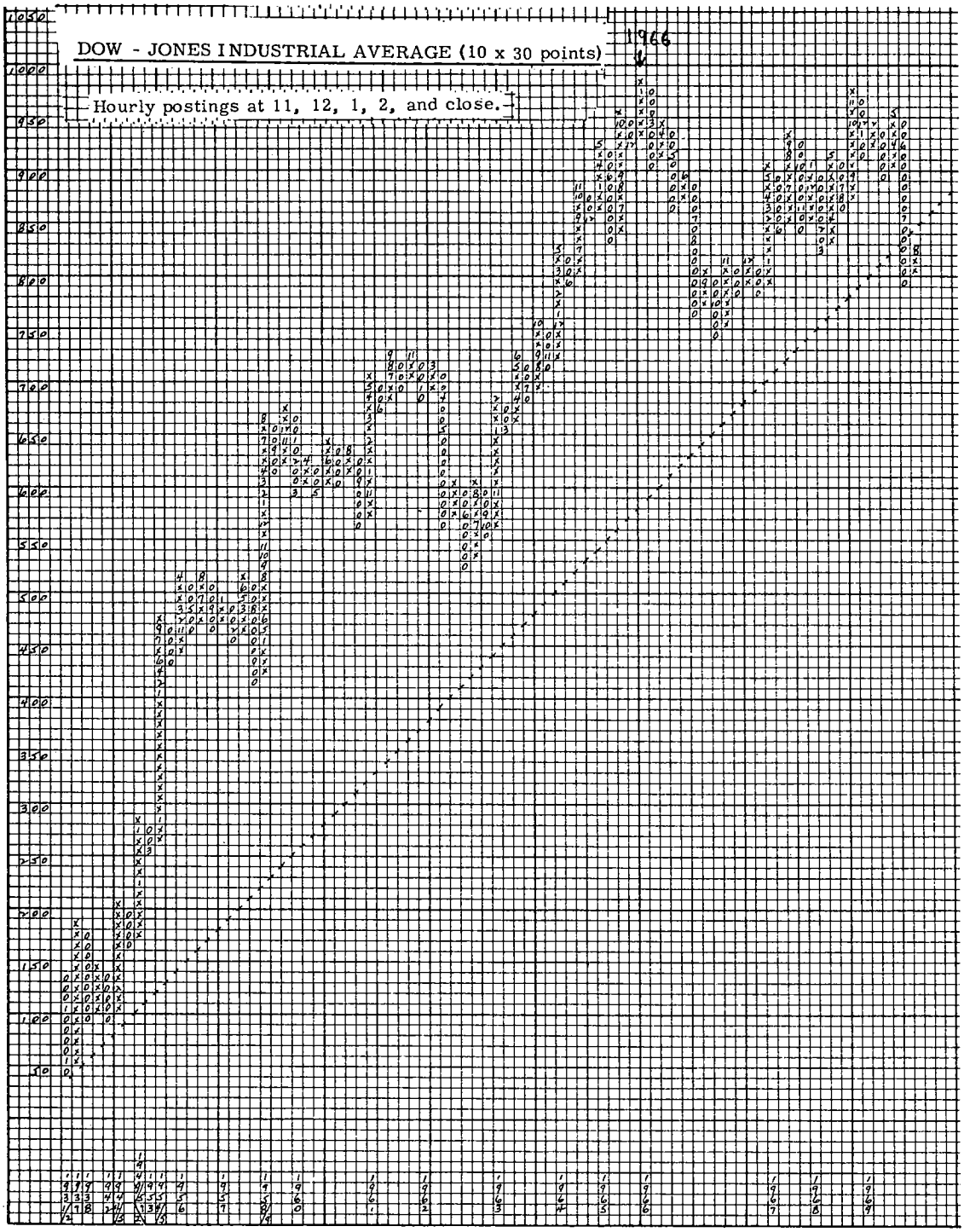
Corporations were restrained in their dividend actions in September, Standard & Poor's Corp. reports.

Of 2,186 dividend actions in September, S& P said, there were 73 increases, down from 102 a year earlier. Extra dividends declined to 44 from 52. Decreases rose to 10 from 6 and omissions increased to 18 from 14.

THIRTY-SEVEN YEARS: The 1969 market action has assumed such great significance that I want again to discuss the big picture. The point & figure chart on page 3 (courtesy of Chartcraft, Larchmont, N.Y.) is a 10 point-30 point reversal chart. This means that each vertical box represents a full 10 points on the Dow Industrial Average, and that only rallies or declines of 30 points or more are shown on the chart. The "X"'s denote rallies, the "O"'s represent declines. The advantage of a P & F chart is compression, the depiction of years of action within a small or compressed space. Only action is shown on a P & F chart-not time. Thus if 7 major rallies and declines occur during a single year, 7 rows of X's and O's will appear for that year. If no rallies or declines occur during a given year, nothing will appear on this chart. For convenience, annual dates are shown at bottom of the chart.

I want to draw subscribers' attentions to a few significant developments on this chart. The first and lowest "O" on the chart is at the 50 level of 1932 (the actual level was 41.22 recorded by the Dow on July 8, 1932, but since the Dow did not decline to an even 40 this 10-point P & F chart shows it as 50). A single ascending trendline has been drawn from the 50 level, and it is apparent that all the movements of the Dow since 1932 have occurred above that bullish trendline.

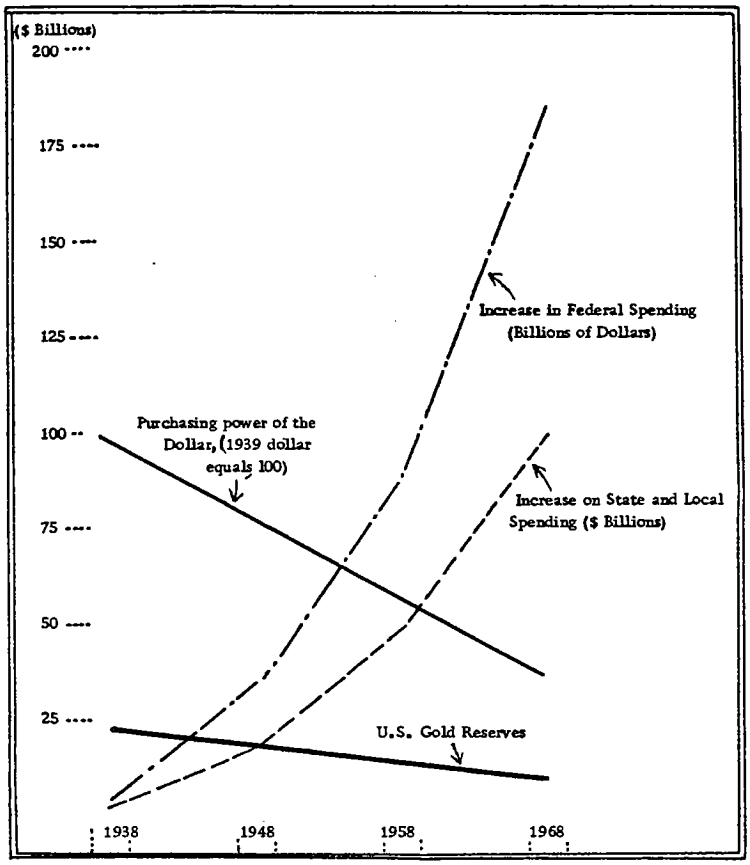
During July, 1969, history was made. It was during that month that the Dow dropped below the 1932-1969 trendline. This took place when the Dow declined below the 840 box on the chart (the great trendline intersected the Dow in July at exactly 840).



A rally began from the 801.96 level of July 29, 1969, and I thought it was significant that the rally halted at the 830 box (the actual termination of the rally was the 837.78 peak of September 2). The rally termination was significant because the Dow was unable to struggle above the trendline, a movement which would have required a rally to 860 on the Dow.

A new decline set in from the September 2 peak. In the last Letter I noted (see end of Letter) that at an hourly reading of 810 on a more sensitive P & F chart the Dow would provide a bearish signal). The Dow dipped below 810 on October 3, thus setting off the bearish signal. On the accompanying less sensitive (long-term) P & F chart, a sell signal will be given on an hourly Dow reading of 800 as this will take the Dow below the preceding "X" or rally beginning. A more authoritative bear signal will be given if the Dow touches 790 on an hourly or a closing basis. A 790 figure would take the Dow into new low territory on this chart, and thereby set the stage for a testing of the 1966 low of 744.32.

All in all, however, I again call attention to the fact that the Dow action is now occurring below the great ascending (or bullish) trendline. This is something which has not occurred in 37 years.



COMPARISONS: Last week I compiled a series of figures and drew a chart. The chart is one of the saddest commentaries on the U.S. economic picture that I have seen. It really speaks for itself, and I wish that everyone could see it and study it (any of my advisory publishing friends may feel free to reproduce this chart without asking permission).

Since 1938 the Federal Government has increased spending from $8.4 billion in 1938 to $188 billion in 1968. States and localities have increased spending from the $9.3 billion of 1938 to $98.9 billion in 1968. Meanwhile, the purchasing power of the dollar has dropped from 100¢ to 38¢ today. During the same period, the U.S. gold stock has dropped from $22 billion to around $10 billion.

Meanwhile, the total of Federal, State and local debt has risen from the $56 billion of 1938 to $370 billion today (and this does not include personal debt). But wait a minute, the total Federal, State and local tax take has rocketed from $14 billion in 1938 to $219 billion today. Doesn't that mean that everything is all right? Tax receipts have zoomed up along with debt, so the old adage of "Tax and spend" seems to be working.

But there is a growing problem. People are about taxed up. Talk of tax revolts is heard around the country. Taxes are getting so high that they are obviously hurting business and the consumer. Where are more taxes to come from? And what happens if a recession hits and tax receipts drop off?

Of course, "it could never happen again," but between 1929 and 1932 the Federal Government's budget receipts dropped from $4.1 billion to $1.9 billion, or more than half. I wonder what would happen if the current Federal tax receipts (1968 was $147 billion for the Government) dropped say 25% to say $130 billion)? Did you know that the interest on the national debt alone is $17.3 billion today? What would happen is that there would have to be a national moratorium on debt payments, the Government would have to flood the money markets with bonds, notes and bills to raise money, and the price of money (interest rates) would go through all known ceilings.

Could all this happen before the primary bear market breathes its last? In my opinion, something very like it could occur. At that time money and gold would be king, profits would be few and far between, common stocks would be in disrepute. During the same period the bear market would be well into its third and final phase and those of us with cash would have a once in a lifetime opportunity to purchase what we want with what nobody had— cash.

SHORT, SHORT: One of the ominous manifestations of the whole picture is the rush of debtors into the short-term market, a rush brought on by the extreme difficulty in capturing long-term money via one of the worst bond markets in history. "He who buys for the long term and borrows for the short term is heading for trouble." This seems to sum up the entire U.S. situation.

I am indebted to my good friend Irving Weiss of Capital Counsellors, 70 Wall St., N.Y.C. for the tabulations listed on page 5. Add to this private short-term debt, which has boomed from about $10 billion in 1960 to about $72 billion today, and you have a total short-term debt rise (public and private) of $87 billion in 1960 to $186 billion today.

Two weeks ago the 91-day Treasury bills rose to a record 7.21% yield, and the reason is obvious. The rush to the short-term market is creating a monstrous traffic bottle-neck as the public and the private borrowers load up with the most expensive debt burden seen since the Civil War.

Short Term Local, State & Federal Debt Within One Year (in nearest Billions of $)

Date	Key Gov't Agcy's	U.S. Gov't	Municipal	Total
1960	5	69	3	77
61	4	80	4	88
62	5	87	4	96
63	5	85	4	94
64	8	81	5	94
65	8	88	5	101
66	11	89	6	106
67	11	90	7	108
68	11	106	8	125
69	14	104	12	130
9/15 69	16	114	14	144

The net result is going to be trouble in financing in all areas. Ultimately it is going to hit car sales, retail sales, housing sales, appliance sales, financing of all types. When we get close to this situation the stock market is going to discount it by plunging as informed investors seek to protect themselves from credit chaos, sliding sales and profits, and a period of financial disaster matching any seen in American history.

NOTES AND INFORMATION: From sources close to the source, this is what I gather the Federal Reserve Board wants: first and most important, the Fed wants a slowing down of economic growth to zero for at least two quarters. The Fed is afraid that only a brief slow-down in the economy and then an immediate opening of the floodgates would make a mockery out of the whole tight money policy. Therefore, the members of the Reserve Board are solidly behind a policy of continuing monetary restraint.

The Fed seems willing to accept (so far) the cave-in on the bond markets and they are willing to accept (so far) the sloppy stock market. The Fed will accept and it looks forward to lower corporate profits and less capital spending.

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In his report of September 29, Joe Granville notes that 68.7% of all Federal and Federal-Agency debt is coming due within the next three years. This backs up what I wrote earlier about the massive and ominous movement of debt into the short-term market. Ultimately (and perhaps very soon) this is going to mean a panic into short-term funds and towards liquidity. The greater the movement of debt (and it is now very great) into the short-term area, the more vulnerable the entire debt structure. Higher cost of debt is being passed on to the consumer in the form of higher prices. The spiraling cycle will ultimarely burst, probably when the consumer cuts back drastically on his buying. Then comes the deluge.

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Harry Schultz,in his report of Sept. 18 talks about his "long-held theory that intelligent men see things as inevitable and act at once, usually not realizing that they are seeing further ahead than they suppose. I have often said great wisdom can sometimes be a short-term handicap on Wall Street. A safe rule-of-thumb which some very bright people have told me privately is that if they estimate something will happen in 6 months, they double it to get the right date." I agree. And that's why bull market tops and bear market bottoms form long before most of us realize that the tide has actually turned. The smart investors knew it, but what they knew takes time, much time to materialize in an obvious way.

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Vietnam is now President Nixon's war. The whole situation is as messy , idiotic and as dishonest as ever. The latest sidelight is the sudden dropping of the "Green Beret Case" reportedly on order from the President. One announced reason for dropping the case: The C.I.A. does not want its agents to testify in court. A more probably reason for dumping the case: The U.S. does not want certain "methods" of the Berets brought out for public airing. Thus, what goes on behind the scenes in the nation's "elite" military corps. will not reach the public at this time.

As to the war itself, I have been saying for over two years that the Communists (from their standpoint) would be crazy to negotiate a war that they are not losing. Concessions and troop withdrawals by the U.S. will not bring them to negotiations, for Hanoi means to win, and they take U.S. concessions as a step along the path to victory. The President's problem is (1) U.S. public opinion, which is against the war, and (2) how to extricate the U.S. from Vietnam without making the withdrawal appear to be what it is— giving up.

My suggestion all along has been— honesty. Fighting the war on the limited (but huge) scale we have been fighting it, did not produce victory. But that policy did take the U.S. to the brink of bankruptcy. Fighting the war with less men will take us further from possible victory. The honest way to pull out would be to admit that the entire affair was a pitiful, ghastly mistake. This, everybody holds, would produce a "loss of face" for the U.S. from which it would never recover.

Instinct tells me that President Nixon doesn't have the vaguest ides of what his Vietnam policy is. The Pentagon wants to fight a winning war, but the American public would never stand for the large-scale effort required. The best hint as to what is now going on may be deduced from this quote by a high Pentagon official: "We are going to reduce the fighting to a level the American public will tolerate for the long pull."

A wag suggests that the U.S. announce that it has "won the war in Vietnam," and then simply pull out. The humor in that statement is the insane seed of truth inherent in the statement. Who knows, we might try that route. In the meantime, dishonesty is the order of the day. Military dishonesty, financial dishonesty, monetary dishonesty, political dishonesty, it's the great disease of our times.

ECONOMIC SCRAPBOOK: Sept. 30.....West Germany, in the wake of a flood of foreign currency speculation, allowed the mark to float free in the exchange markets. The effect was an immediate 4% boost in the value of the market. In reality, the move violated the I.M.F. rules of a 1% allowable fluctuation. Construction contracts confounded economists by spurting $6.5 billion in August. The bellwether 4¼ Treasuries of 1987-92 broke below 71 for the first time since their issuance in August, 1962.

Oct. 2.....The W. German mark rose 5.25% above its official value as speculative money poured in to purchase marks. Thirteen N.Y. savings banks stated that outflow on two critical September days doubled over the 1968 period with a loss of $86 million for the two days.

Oct. 3.....Factory orders declined 1.8% in August. All industries were affected. Despite the two-tier ban, central banks have purchased $100 million in gold from S. Africa it was learned. The Fed kept a tight rein on credit with borrowed reserves last week at minus $1.2 billion, up from $903 million the week before. Consumer credit rose $600 million in August, smallest increase in 19 months.

Oct. 6.....76% of purchasing agents reported price increases, this figure equalling a 13-year record. Andrew Brimmer of the Fed called for continued monetary rightness, saying that "there appears to be a real prospect that inflationary pressures will persist on into the early months of next year.

Oct. 7.....Unemployment jumped .5 to 4%, the sharpest rise in nine years. The French franc dropped to a post-devaluation low, raising fears of another franc devaluation unless the German mark is re-valued upwards.

STOCKS: I have been reviewing the daily charts of almost all stocks on the N.Y.S.E. My conclusion is discouraging: Too many issues are just not holding. Declining days are accompanied by too many new lows for the year, with given days bringing in new lows on 10% and 15% of all listed issues. New highs failed to outnumber new lows on a single day of the rally since July 29, 1969. That's just not good enough.

I include a typical chart of a big company, Bethlehem Steel (this daily chart courtesy of Traders Research, 101 Cherry St., Alton, Ill. 62002). The arrow points to the July 29 low, the day that the Dow Industrial Average hit its 1969 low of 801.96. Note that Beth Steel just couldn't hold. This great company (America's second largest steel company), now selling below book value, is heading for a test of the 26 area. If it breaks 26, it will have sunk to a 14 year low. And that readers, is primary bear market action.

LATE NOTES (Thurs. morn., Oct. 9): As this is written the Industrials are down 2 points to just below the 1969 low of 801.96. Rails are still a point away from their own 1969 low of 193.19. A closing below the two 1969 lows of 801.96 and 193.19 by the two Averages will reconfirm the primary downward trend. There is now widespread talk of a "false" downside breakout if the lows are penetrated. New lows could prove to be a false signal, but at this stage in the bear market I wouldn't bet on it (which means buying stocks). I'll leave that to the geniuses and the perpetual optimists.